American Bar Association Response to
Follow-Up Questions from Senator Kohl for Hearing on "The Discount Pricing Consumer Protection Act: Do We Need to Restore the Ban on Vertical Price Fixing?"

Thank you again for the opportunity to testify on behalf of the American Bar Association in the Subcommittee's hearing. Below I have tried to answer the questions you raised in your letter of June 1, 2009.

1. You testified that you did not believe that ending the per se ban on vertical price fixing would lead to higher prices. But there is substantial evidence that vertical price fixing in fact leads to higher prices. For 40 years prior to 1975, federal law permitted states to enact so-called "fair trade" laws allowing vertical price fixing. These laws were abolished by the passage of the Consumer Goods Pricing Act of 1975. Numerous studies prior to the passage of that law in 1975 documented the fact that retail price maintenance leads to higher prices. Studies conducted by the Department of Justice in the late 1960s indicated that retail prices were between 18 and 27 % higher in states that allowed vertical price fixing than those that did not. And, in his dissenting opinion in the Leegin *case, Justice Breyer estimated that if just ten percent of products were subject to vertical price fixing, would affect $ 300 billion dollars in commerce, raising the average bill a family of four would pay for retail goods by $ 750 to $ 1000 every year. What is your response to all of this evidence?*

Response: The studies to which you referred are among many that have been conducted on the effects of vertical price fixing, and others studies have reached different results. Collectively, the studies show that minimum resale price maintenance can have mixed effects – in some instances it can be procompetitive, and in other instances it can have anticompetitive effects that produce higher prices. Because resale price maintenance can be benign or procompetitive, rule of reason analysis is the appropriate way of measuring these mixed effects. If resale price maintenance produces anticompetitive effects, it can be found unlawful under the rule of reason.

Many economic studies have reported or predicted that resale price maintenance will lead to higher prices, but those studies that are based on analysis of actual market effects all use data from the fair trade era – from passage of the Miller-Tydings Fair Trade Act in 1937 to passage of the Consumer Goods Pricing Act of 1975. These studies, which include those to which you referred in your question, were summarized in a 1983 staff report of the Federal Trade Commission's Bureau of Economics prepared by Thomas R. Overstreet, Jr.[1] The results are actually far more equivocal than has been portrayed by supporters of a return to the *per se* rule for minimum resale price maintenance.

Several of the studies reviewed by Overstreet showed that resale price maintenance had mixed effects. In a 1938 study of 50 drug products sold by drug retailers in New York State, the data showed that, after passage of fair trade legislation, prices increased for nationally advertised

[1] THOMAS R. OVERSTREET, JR., RESALE PRICE MAINTENANCE: ECONOMIC THEORIES AND EMPIRICAL EVIDENCE (F.T.C. 1983).

goods sold in discount stores, but fell slightly for the same items sold in non-discount stores.[2] Prices for those items that were not nationally advertised did not seem to be affected.[3]

In a study of the effects of the 1970 repeal of fair trade legislation in Rhode Island, retail prices on five of the nine product lines surveyed were not affected by repeal.[4] For the four product lines that showed price declines, price reductions were not universally implemented. Many smaller retailers simply held their prices unchanged and reduced their inventories and selections from the product line.[5]

In a 1945 FTC study of pricing for drug and food products in selected cities, the data showed that use of resale price maintenance had mixed results. After passage of fair trade laws, prices of vegetable oil shortenings increased in chain and department stores but declined in individual stores.[6] Prices of soap products and cake flour increased in supermarkets but fell in individual stores, and for other grocery products there was no observable change in prices.[7] For products sold through retail drug stores, the data showed that prices decreased at individual stores in medium-sized and large cities.[8]

Overstreet concluded that resale price maintenance can have diverse effects,[9] and the empirical evidence indicates that it did not, during the fair trade era, lead uniformly to higher retail prices for consumers. We question the value of the fair-trade-era studies because they are dated and took place under very different circumstances. They should not, in any event, be used in making predictions about resale price maintenance in the current marketplace, for the following reasons.

First, fair trade laws were not equivalent to an antitrust regime that provides rule of reason treatment for resale price maintenance. Resale price maintenance in today's economy depends on the willing acquiescence of both seller and retailer; under the fair trade laws of certain states, a resale price maintenance agreement with *one* retailer in a state could bind all other retailers, whether they agreed or not.[10] The competitive effects of that regime would obviously be very different from those flowing from a resale price maintenance agreement between a manufacturer and its dealers today.

Second, the retail landscape in the U.S. is considerably different today than during the fair trade era, and it is improbable that a manufacturer could impose resale price maintenance on big box discount stores like Wal-Mart, Target or Best Buy unless the stores were satisfied that the pricing was competitive. These types of large multi-brand retailers, which account for a significant part of the consumer economy,[11] have buying power that "trumps even the power of a

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[2] *Id.* at 107.
[3] *Id.*
[4] *Id.* at 127.
[5] *Id.* at 128.
[6] *Id.* at 137.
[7] *Id.*
[8] *Id.* at 137-38.
[9] *Id.* at 163.
[10] *See* 1A CALLMANN ON UNFAIR COMPETITION, TRADEMARKS AND MONOPOLIES § 6:3 n.4 (4th ed. 2007).
[11] Wal-Mart is said, for example, to account for 22% of all toys sold in the U.S. *See* Warren S. Grimes, *Buyer Power and Retail Gatekeeper Power: Protecting Competition and the Atomistic Seller*, 72 ANTITRUST L.J. 563, 580 (2005).

supplier of a major brand."[12] As one commentator has noted, this kind of retail buying power gives the large retailer control over "whether [items] will be *priced* or marketed aggressively," and this, in turn, gives it "substantial leverage in dealing with even the largest producers of strong brands of consumer products."[13] To the extent that empirical studies from the fair trade era indicate that resale price maintenance resulted in higher prices, the findings cannot be extrapolated to support predictions about what the effects would be in the current economy.

Sale of branded goods through off-price discounters has become such a deeply embedded retail channel that off-price discounters, similarly, are not likely to be affected by the change in treatment of minimum resale price maintenance from *per se* to rule of reason. This was suggested in a July 6, 2007 article in USA TODAY that looked at the effect of *Leegin* on the sale of discounted apparel brands.[14] The authors concluded that the impact of the Court's decision on off-price retailers was "likely to be slight," and we have seen no studies or analyses that would suggest that the Court's approval of rule of reason treatment for resale price maintenance has had any effect on availability of goods through off-price retailers, whether selling apparel or other goods.

Nor are there any studies of which we are aware analyzing the effects of resale price maintenance agreements on consumer prices since the *Leegin* decision. One of the witnesses before the Subcommittee, Stacy John Haigney, stated that his employer, Burlington Coat Factory, has experienced no negative impact from the decision.[15] He suggested that the weak economy may have "temporarily divested manufacturers of the power to dictate retail prices,"[16] but, whatever the explanation, there is no empirical evidence that the Court's decision has had any observable impact on retailers.

The baseline question is whether consumer welfare will be adversely affected by a change in how minimum resale price maintenance agreements are evaluated under the antitrust laws. While some manufacturers may find it advantageous to use such agreements to ensure that retailers provide amenities (e.g., atmosphere, convenient downtown locations – all of which are expensive) or services, any such agreements will have their effect on intrabrand competition among those selling a manufacturer's product.

2. Under the Colgate *doctrine a manufacturer is free to refuse to allow any retailer to sell its products. This doctrine would be unchanged by S. 148, the Discount Pricing Consumer Protection Act. Doesn't the availability of the* Colgate *doctrine satisfy any concern that reinstating the rule against vertical price fixing would prevent manufacturers from limiting the distribution of their products to store that provide the support and technical expertise that manufacturers require?*

According to the Corporate Fact Sheet on its website, http://walmartstores.com/FactsNews/FactSheets/, (viewed June 9, 2009), Wal-Mart had 4100 facilities in the U.S. as of July 17, 2008.

[12] Grimes, *supra* note 11, at 579.

[13] *Id.* (emphasis added).

[14] Jayne O'Donnell & Christine Dugas, *Discounted Designer Labels Here to Stay; High Court Ruling Unlikely to End Off-Price Retailing,* USA TODAY, July 6, 2007, at B1.

[15] Statement of Stacy John Haigney at 12 (May 19, 2009).

[16] *Id.*

Response: Implicit in the reasoning of the ABA Resolution supporting the application of the rule of reason to resale price maintenance agreements is the view that the availability of the *Colgate* doctrine does not satisfy the concern that a per se rule against vertical price fixing could prevent manufacturers from limiting the distribution of their products to stores that provide the support and technical expertise that manufacturers require. Manufacturers that seek to institute *Colgate* programs are faced with considerable practical difficulties in administering them. These difficulties are largely driven by the necessity of avoiding any conduct that could be seen as being tantamount to an agreement between a manufacturer and a retailer. A useful portrayal of the contortions associated with *Colgate* programs is contained in the *amicus curiae* brief of PING, Inc. ("PING") filed in the *Leegin* proceedings (the "PING Brief"). There, PING, a manufacturer of golf equipment, described the administration of its *Colgate* policy as follows:

> To minimize the risks created by *Colgate*, PING drastically restricts employees' communications with the retailers to whom they sell and, worse, summarily terminates retailers for even the smallest policy violations, without considering whether the violation was intentional or why it occurred. PING employees as many as 12 full-time people who work on the *i*FIT Pricing Policy [which contained PING's *Colgate* policy] and related matters and has spent millions of dollars on the administration of the Policy since 2004.[17]

PING further noted that in order to avoid the possible characterization of any discussion with retailers as an agreement, no PING employees (including sales representatives), with the sole exception of in-house counsel, were permitted to engage in any communication concerning the company's *Colgate* policy. Indeed, PING noted that this created "substantial frustration" for its retail accounts, who were simply unable to communicate with their primary PING contact about any aspect of the policy, and were directed to deal with PING's counsel instead. One of PING's retailers described how this worked in practice:

> And, when [my PING Sales Representative] originally brought this policy to us in 2004(?) it was the most bizarre presentation ever. He handed it to me. I looked at it and tried to ask questions . . . all he kept saying was "I CAN'T TALK ABOUT PRICE" – "I CAN'T TELL YOU ANYTHING ABOUT THAT" . . . about 3 or 4 times. I tried to ask different questions about it, but he couldn't or wouldn't talk about it. I felt left alone to fend for ourselves.[18]

In the event that PING retailers contacted the company's in-house counsel to discuss aspects of the *Colgate* policy, they would often receive the following formalistic response:

> I recognize that the questions you asked, and the information you provided, in your email are not in any way intended to indicate any approval, agreement or any other assurance of compliance with respect to the *i*FIT Pricing Policy. However, if that was in any way your intent, please note that it is, and always will be, expressly rejected by PING. PING specifically provides at Section II of the *i*FIT Pricing Policy that: "PING does not seek, and will not accept, any account's

[17] PING Brief, p. 10.
[18] PING Brief, page 12.

> approval, agreement or any other assurance of compliance with respect to this *i*FIT Pricing Policy and/or the Orange & Blue List." You need to decide on your own what you charge for the PING products you sell.[19]

The arrangements made by PING in dealing with its *Colgate* policy are not unique. Prior to the decision in *Leegin*, many other manufacturers in a broad range of industries had instituted similar measures which, in sum, did not achieve a pro-competitive purpose or enhance consumer choice or efficiency in any way. As a result, it cannot clearly be said that the availability of the Colgate doctrine satisfies the concerns associated with reinstating the rule against vertical price fixing in this regard.

3. Defenders of the Leegin decision point out that the majority opinion in Leegin still permits antitrust suits against vertical price fixing if the party bringing the suit can prove that the practice was "unreasonable" and harmed competition. This is what is known in antitrust law as the "rule of reason."

You are an experienced antitrust lawyer, Mr. Wilson. What kind of showing would a plaintiff have to make to prevail in rule of reason case challenging vertical price fixing?

Among other things wouldn't the plaintiff have to show market power of the manufacturer imposing minimum retail prices? Wouldn't the plaintiff have to bring forward extensive economic studies detailing the effect on the market? How realistic is it for a smaller retailer competitor to have the resources to do this?

Response: A plaintiff in a resale price maintenance case must show that the restraint has anticompetitive effects that outweigh any procompetitive effects of the restraint. It is not novel or unrealistic to expect a plaintiff to establish market power or actual anticompetitive effects. Plaintiffs have long been required to meet this burden through economic evidence when challenging other vertical restraints, such as tying, exclusive dealing, territorial restrictions and price discrimination, and the plaintiffs' antitrust bar has shown itself to be well equipped and highly experienced in the use of economics experts.

4. Mr. Wilson, you represent the American Bar Association. Do you or your organization believe a Supreme Court decision is an appropriate way to reverse a century-old antitrust rule repeatedly reaffirmed by Congress? Does the Supreme Court have the economic expertise and the fact finding capability to make such a change in law, or such a matter better left to the legislative branch?

Response: The ABA has not adopted a position as to whether the courts or Congress is better equipped to weigh and evaluate economic evidence. The ABA Policy upon which I testified was adopted prior to the *Leegin* decision, and supported reversal of *Dr. Miles*, and adoption of a rule of reason test. As noted in my testimony, the economic literature weighs heavily against condemning all minimum resale price agreements to per se illegality. Notable examples include Robert H. Bork, The Antitrust Paradox 32 (1978), and Richard A. Posner, Antitrust Law 189 (2d ed. 2001). *See generally* ABA SECTION OF ANTITRUST LAW, ANTITRUST LAW AND ECONOMICS

[19] PING Brief, page 13.

OF PRODUCT DISTRIBUTION 37-76 (2006) ("the bulk of the economic literature on [minimum resale price maintenance] . . . suggests that [minimum resale price maintenance] is more likely to be used to enhance efficiency than for anticompetitive purposes"). The seminal treatment appears in Lester G. Telser, *Why Should Manufacturers Want Fair Trade,* 3 J. L. & ECON. 86 (1960), which explained why manufacturers would adopt minimum resale price maintenance to assure the efficient distribution and marketing of their products—by encouraging dealers to promote the product without fear of "free riding" by rival dealers of the same brand that cut prices and spend little or nothing on services. As this principle is described by Judge Posner, when dealers are forced to compete without cutting prices, they "vie with one another to provide presale services" and the manufacturer benefits. Richard A. Posner, *Legal Narratology,* 64 U. CHI. L. REV. 737, 738 (1997). The prevailing view among economists is that minimum resale price maintenance is more often adopted to serve the interests of manufacturers in achieving efficiencies in distribution than to serve the interests of dealers in assuring their margins. *See Business Electronics Corp. v. Sharp Electronics Corp., supra,* at 727 n. 2 ("[r]etail market power is rare" *citing* Baxter, *The Viability of Vertical Restraints Doctrine,* 75 Calif. L. Rev. 933, 948-49 (1987)).

5. Is there any legislation you believe might be appropriate to limit vertical price fixing, or are you completely satisfied with the state of the law following the Leegin decision? Specifically, do you support proposals to retain a rule of reason approach to vertical price fixing, but to apply a presumption against the legality of the restraint?

Response: The ABA has no position on alternate legislation but is prepared to review and perhaps comment on any such legislation that may be introduced. The ABA, and/or the ABA Section of Antitrust Law, as appropriate, plans to provide its input to the Federal Trade Commission as it explores the appropriate rule of reason approach in resale price maintenance cases.

6. Virtually every other western industrialized democracy treats vertical price fixing as per se illegal, including Great Britain, Germany, France and many others. What does this experience teach us?

Response: ABA has no position on the resale price maintenance rules of other countries, but notes that the standards are not as uniform as the question suggests. In fact, the United Kingdom, France and Germany actually do not apply what the U.S. would consider a per se test in evaluating resale price restraints – the test they apply arises out of European competition jurisprudence, and allows the party imposing the restraint to demonstrate its efficiencies. *See* Luc Pepperkorn, "Resale Price Maintenance and Its Alleged Efficiencies" 4 European Comp. J. 201 (2008). More fundamentally, our antitrust laws are not patterned after those of other countries because the U.S. had antitrust laws in place, with a rich and responsive body of judicial decisions, long before these other countries did. Experience has shown that the antitrust laws of the European Union and its member nations have been converging with those of the U.S., not the other way around. One reason is that because the U.S. antitrust laws have been in place for such a long period of time, these and other countries can learn from the long term U.S. experience.

Over the years, the antitrust laws of many foreign countries have moved closer to U.S. law. For example, the European Commission has adopted rules of antitrust analysis that closely resemble U.S. law, such as with respect to market definition and merger analysis. So has the United Kingdom ("U.K.") Thirty years ago, the U.K. blocked enforcement of U.S. antitrust law (even cartel law) against its nationals. Today, the U.K. prosecutes cartels criminally and has extradited U.K. citizens in the U.S. for criminal prosecution for cartel conduct.

The Court's decision in *Leegin* does not depart from the basic tenet that protection of competition is the goal of the antitrust laws. Instead, it has freed one type of restraint -- minimum resale price maintenance agreements -- from a rigid rule that had prevented any inquiry into whether such a restraint could prove beneficial to competition and consumer welfare in certain cases. If other countries continue to follow more rigid rules than the U.S. regarding resale price maintenance agreements, that is their prerogative, but their experience does not necessarily offer meaningful guidance on how U.S. antitrust law should be applied. But it is equally possible, and perhaps more likely, that other jurisdictions will follow the lead of the U.S. with respect to resale price maintenance as they have with respect to other antitrust laws.